

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce Street

MS:4920:DAL

Dallas, TX 75242

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

Date: March 28, 2008

Number: **200829045**

Release Date: 7/18/2008

LEGEND

ORG = Organization name

XX = Date

Address = address

UIL: 501.03-01

ORG

Person to Contact:

ADDRESS

Contact Telephone Number:

In Reply Refer to: TE/GE Review Staff

EIN:

LAST DATE FOR FILING A PETITION

WITH THE TAX COURT: June 26, 20XX

CERTIFIED MAIL

Dear _____ :

This is a Final Adverse Determination Letter as to the ORG exempt status under section 501(c)(3) of the Internal Revenue Code.

Our adverse determination was made for the following reasons:

A substantial part of your activities consists of providing down payment assistance to home buyers. To finance the assistance, you rely on home sellers and other real-estate related businesses that stand to benefit from these down payment assistance transactions. Your receipt of a payment from the home seller corresponds to the amount of the down payment assistance provided in substantially all of your down payment assistance transactions. The manner in which you operate demonstrates you are operated primarily to further your insiders' business interests. Therefore, you are operated for a substantial nonexempt purpose. In addition, your operations further the private interests of the persons that finance your activities. Accordingly, you are not operated exclusively for exempt purposes described in section 501 (c)(3). In addition, you have failed to meet the requirements of Internal Revenue Code section 501 (c)(3) and Treasury Regulation section 1.501 (c)(3)-1(d)(ii) in that you have failed to provide information to establish that you were not operated for the benefit of private interests.

Based upon these reasons, we are retroactively revoking your IRC section 501(c)(3) tax exempt status to October 10, 20XX. Contributions to your organization are no longer deductible under section 170 of the Internal Revenue Code.

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending December 31, 20XX, and for all years thereafter.

Processing of income tax returns and assessment of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination in court, you must initiate a suit for declaratory judgment in the United States Tax Court, the United States Claim Court or the District Court of the United States for the District of Columbia before the 91st day after the date this determination was mailed to you. Contact the clerk of the appropriate court for the rules for initiating suits for declaratory judgment.

You also have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers.

You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling (404) 338-8099, or writing to:

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

We will notify the appropriate State Officials of this action, as required by section 6104(c) of the Internal Revenue Code.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

Marsha A. Ramirez
Director, EO Examinations

Enclosure:
Form 886-A



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service

November 20, 2007

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear ,

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

ISSUE

Whether ORG operated exclusively for exempt purposes within meaning of section 501(c)(3)?

FACTS

ORG (ORG) is a XYZ not-for-profit corporation incorporated on December 27, 20XX. President is ORG's Registered Agent and President. ORG's address is Address.

On December 4, 20XX, ORG applied for recognition as a tax-exempt organization under section 501(c)(3). On October 10, 20XX, based on the information that ORG provided in its application for exemption and on the assumption that ORG would operate in the manner represented in its application, ORG was recognized as a tax-exempt organization as described in section 501(c)(3).

Since 20XX, ORG has promoted and operated a down payment assistance program for home buyers under which it provides funds to the buyers to use as their down payment and collects the same amount, plus an additional fee, from the home sellers. As more fully described below, under ORG's down payment assistance program, assistance is provided to buyers without income or asset limitations.

Form 1023, Application for Recognition of Tax-Exempt Status

ORG filed Form 1023 with the IRS to apply for recognition of tax-exempt status on December 3, 20XX. On its Form 1023, ORG detailed the following activities:

The Organization's primary objective is to increase home ownership among individuals and families unable to save enough money for a down-payment. To facilitate this objective, the Organization will provide gifts to be used as down-payments for homes in an amount of approximately three percent (3%) of the purchase price. The buyer is also encouraged (but not required) to participate in a home ownership education course. The Organization is funded primarily through collecting a service fee from the sellers or builders of the homes which are purchased by participants in the Organization's program.

The down-payment gifts will be available to anyone on a non-discriminatory basis if he or she makes a proper application to the Organization. The down-payment gifts will be made with no expectation of repayment.

The Organization hopes to increase home ownership by offering assistance to individuals and families who are unable to save enough money for a down-payment. The Organization believes that home ownership benefits individuals and their communities by creating pride and a sense of belonging. The Organization has two mottos: Motto and Motto. The Organization will work to implement these mottos through its programs.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

In addition to the down-payment assistance program, the Organization will sponsor classes and seminars on the benefits and responsibilities of home ownership. The Organization will publicize its services through radio and newspaper advertising. In addition, the Organization will work with other community organizations and out-reach programs to target individuals and families who will benefit from the programs.

Regarding the organization's sources of financial support, ORG's Form 1023 listed the following sources:

The Organization's primary source of financial support will be from the service fees collected from sellers and builders whose homes are purchased by the participants. Other sources will include donations from other charitable foundations and organizations. If necessary, the Organization may apply for grants or other funding from other sources.

Regarding fundraising and contributions, the application states the following:

The Organization's fundraising program has been started. The Organization has received commitments of support from a few organizations. The main method of fundraising will be personal solicitation by an employee of the Organization or a volunteer. This person will meet with potential donors and explain the programs offered by the organization. If the need arises, the Organization may form a committee to solicit donations.

On February 13, 20XX, the IRS requested additional information from ORG regarding its application. A letter was sent to the organization which stated:

Based upon the information submitted and applicable law, it appears you may not qualify under section 501(c)(3) of the Code. We reach our conclusion for the reasons discussed below.

First, you indicate an important part of your operation, and your primary source of income, will be the performance of services to persons attempting to market their homes in exchange for a fee comprised of a percentage of the final sales price. There is no information from which it can be concluded that the services you describe will further or advance any charitable purpose. It appears the described services provide a convenience and a benefit to homeowners who are not members of a charitable class of persons. Because services you describe further no exempt purpose, and because they result in benefits to private persons, you do not meet the operation test of section 501(c)(3) of the Code which requires that you operate exclusively for charitable purposes.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

Secondly, you indicate another important part of your operations will be providing financial benefits to persons of low and moderate income to assist them in acquiring a home. While the providing of assistance to low income, or needy individuals to enable them to acquire housing would otherwise be considered a charitable activity, providing these benefits to moderate income persons would not be deemed charitable. You have not explained how benefits you propose to provide to moderate income persons further a charitable purpose and you have, therefore, not described activities that are exclusively charitable in compliance with the requirements of section 501(c)(3) of the Code.

The letter also advised ORG regarding action to take in the event that it disagreed with the Service's findings. In part, the letter states the following:

Also, if you disagree, please provide the following:

- 1.) A copy of your original filed Articles of Incorporation
- 2.) Rev. Proc. 96-32 provides guidelines for determining whether organizations providing housing are described in section 501(c)(3) of the Code.

Specifically address the following:

Will you agree that for each housing project that (a) at least 75 percent of the units will be occupied by residents that qualify as low-income; and (b) either at least 20 percent of the units will be occupied by residents that also meet the very low-income limit for the area or 40 percent of the units will be occupied by residents that also do not exceed 120 percent of the area's very low-income limit? Up to 25 percent of the units may be provided at market rates to persons who have incomes in excess of the low-income limit.

If you agree, please submit a resolution adopted by your governing body and signed by at least (2) officers agreeing to the above."

On March 20, 20XX, ORG provided its response to the request for additional information. ORG disagreed with the IRS's findings. The organization's response states the following regarding the IRS's conclusion that performing services for those persons attempting to market their homes does not further or advance any charitable purpose:

In your letter, you concluded that an important part of the Organization's operation will be the performance of services to persons attempting to market their homes in exchange for a fee comprised of a percentage of the final sales price. This is incorrect. The Organization's primary function will be to offer down payment assistance in the form of gifts to participating

Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

individuals (the "Program") as explained below.

- a. An individual or family that is interested in purchasing a home will apply to become a Program Participant (a "Participant").
- b. A Participant will then select a home from Program-qualified homes, as described below.
- c. At the time the Participant closes on the purchase of the Program-qualified home, the Organization will make a gift to the Participant in an amount up to three percent (3%) of the purchase price of the Program-qualified home to be used as part or all of the down payment for the Program-qualified home. The Organization will deliver the amount of the gift on behalf of the participant directly to the closing agent.
- d. Program-qualified homes are those homes that a builder/seller has made available for the Program and on which the builder-seller has agreed to pay to the Organization a fee at the closing on the program-qualified home, equal to four percent (4%) of the purchase price. This fee will be placed in a pool of funds for use by the Organization for down-payment assistance for participants.

To the extent that the services provided under the Program benefit the builders/sellers, the benefit is simply a by-product to the services provided to the participants. As a result of the services being provided to the charitable class of persons, the seller/builder may receive an ancillary benefit through the increase in the number of qualified buyers who may purchase the home. However, the Organization does not guarantee the sale of a qualified home or offer any additional service to the builder/seller.

Regarding The IRS's conclusion that providing down-payment assistance to moderate income persons would not further a charitable purpose, ORG's response stated:

In your letter, you also indicate that providing benefit to moderate-income persons would not be deemed charitable. This is incorrect. The Organization's board of directors has approved a resolution (a copy of which is enclosed) whereby the Organization agrees to follow the guidelines set forth in Revenue Procedure 96-32. Revenue Procedure 96-32, which establishes a safe harbor for qualification as tax-exempt under Section 501(c)(3), allows a percentage of participants in a program that qualifies under the safe harbor to have income in excess of the low-income limit. Therefore, as long as the Organization is in compliance with Revenue Procedure 96-32, the Organization qualifies for tax-exemption. The Program can provide benefits to moderate-income persons under Revenue Procedure 96-32.

As a part of its response, ORG included a resolution adopted by the board of directors and signed by the President on March 20, 20XX, which outlined its intent to comply with Revenue Procedure 96-32. The resolution states:

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name

XX = Date

XYZ = State

President = president

Address = address

Motto = motto

RESOLVED, that the Board of Directors agrees to follow the guidelines set forth in Revenue Procedure 96-32 as follows:

1. At least seventy-five percent (75%) of the Participants who receive down payment gifts through the Program will qualify as low-income; and
2. Either (a) at least twenty percent (20%) of the Participants who receive down payment gifts through the Program will meet the very low-income limit for the area or (b) forty percent (40%) of the Participants who receive down payment gifts through the Program will not exceed one hundred and twenty percent (120%) of the area's very low-income limit.

Up to twenty-five percent (25%) of the Participants who receive down payment gifts through the Program may have income in excess of the low-income limit.

On June 3, 20XX, the IRS again concluded that ORG may not qualify for exemption under section 501(c)(3) of the Code. The reason given states:

You indicate an important part of your operation, and your primary source of income, will be the performance of services to persons attempting to market their homes in exchange for a fee comprised of a percentage of the final sales price. There is no information from which it can be concluded that the services you describe will further or advance any charitable purpose. It appears the described services provide a convenience and a benefit to homeowners who are not members of a charitable class of persons. Because services you describe further no exempt purpose, and because they result in benefits to private persons, you do not meet the operational test of section 501(c)(3) of the Code which requires that you operate exclusively for charitable purposes.

On June 6, 20XX, The IRS again requested additional information from ORG in order to process the organization's application for exemption. ORG was asked to provide a statement indicating that it has no relationship with any real estate professional; it was also asked to sign an agreement indicating it would not require a fee from sellers participating in the DPA program.

On June 24, 20XX, ORG responded with a letter from its representative. The letter includes the two statements below:

ORG, Inc. submits that no member of its Board of Directors will receive any financial benefit from the sale of such homes.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

Therefore, ORG, Inc. agrees that it will not in the future require the sellers to pay any percentage of the purchase price of the qualified home at closing to ORG, Inc. However, ORG, Inc. reserves the right to change its position based on an IRS ruling, finding, or any court decision concluding the payments by the sellers under similar facts do not affect the tax-exempt status of the nonprofit organization.

On October 10, 20XX, Letter 1045 was issued to ORG, Inc. granting them exempt status as a 501(c)(3) organization. The advance ruling period began on June 24, 20XX and ended on December 31, 20XX.

Federal Returns

ORG filed Forms 990 for the calendar years ended December 31, 20XX, 20XX, 20XX and 20XX: it did not file Form 990-T. Form 990 for the year under examination (20XX) was filed on November 16, 20XX. ORG did not file Forms 941, W-2, or 1099-MISC, although its return for the year under examination does indicate that ORG paid salaries and wages in the amount of \$.

In 20XX, ORG's reported activities consisted of operating its down payment assistance program as described in more detail below.

ORG's Form 990 for 20XX includes an attached statement for Part III, which explains the organization's primary exempt purpose; ORG reported its Program Service Accomplishments with related expenses as follows:

ORG, Inc. is an affordable housing company, created to provide a means to increase home ownership among individuals and families unable to save enough money for a down payment. This purpose is facilitated by complying with FHA guidelines, to gift down payments to anyone purchasing a home with a FHA loan. The down payment is a gift from ORG, Inc. with no expectation of repayment, in any form of money or services. The gifts of the down payment monies are available to anyone on a non-discriminatory basis.

During 20XX ORG, Inc. provided over \$ in gifts to 151 individuals and families.

In 20XX, ORG received \$ in gross revenue from amounts paid to it by sellers participating in ORG's DPA program. ORG reported the seller's payments as Program Service Revenue. ORG also reported that it distributed \$ in down payment assistance to homebuyers for use as down payments and/or to pay for closing costs in 20XX. ORG also made charitable contributions to other organizations in the amount of \$ for 20XX. ORG's Form 990, Part IV,

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

line 73, shows that as of December 31, 20XX, ORG had total unrestricted/net assets of \$.

Operation of ORG's Down Payment Assistance Program

ORG provided limited information regarding the operation of its down payment assistance program. No website for the organization was located; ORG did not provide copies of any of its promotional materials such as flyers, brochures, magazines, newsletters or other promotional materials after repeated requests. Based on the financial documents provided, ORG received all of its funding for its down payment assistance program from builders. On its Regular Trial Balance, ORG recorded the total amount it received each month from builders as "Revenue: Builders Contributions". This amount represents the total amount paid monthly to ORG by builders who sold homes through ORG's Homebuyer Assistance Program. ORG also provided a monthly Transaction Listing which reports, for each sale, the amount paid to ORG by the builder (the amount of the down payment assistance plus the service fee) and a corresponding transaction which records the amount paid to the closing attorney on behalf of the buyer (the amount of the down payment assistance only). The Transaction Listing verifies that the amount paid to ORG is for a particular home buyer as the buyer's name is listed with each transaction. Therefore, it is apparent that the builder intends for the monies to be designated for a specific home buyer. Based on the documents provided, the amount contributed to ORG on behalf of each buyer is 4-5% of the contract sales price, while the amount of down payment assistance provided to each buyer by ORG is 3% of the contract sales price. On the HUD settlement statement, the down payment assistance provided to the home buyers is recorded as "Opening Doors Gift Funds".

ORG did not provide any information indicating whether the buyers in ORG's down payment assistance program utilize Federal Housing Administration (FHA) financing and/or conventional financing for their home purchases. ORG refused to provide copies of any of its agreements, applications, forms and/or other documents utilized in the DPA program. ORG also refused to provide copies of any documents completed and/or signed by the buyers, sellers, realtors, and/or others involved in the down payment assistance transactions.

However, based on the documents ORG did provide, it is evident that these transactions result in a circular flow of money. The sellers/builders make payments to ORG. ORG provides the funds to the buyers, who use the funds to make the down payment necessary to purchase the sellers/builders homes.

Despite the representations in its application for exemption and additional representations when asked for additional information in connection with the application, ORG does not have income limitations for its down payment assistance program and did not screen applicants for down payment assistance based on income. The records provided by ORG did not include data on the

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

buyers' incomes. Rather, ORG's down payment assistance program provided "gifts" to any homebuyers who qualified for a loan. In fact, the 20XX Form 990, Part III states the following:

The gifts of the down payment monies are available to anyone on a non-discriminatory basis.

ORG did not provide any information to verify that it made any attempts to comply with Revenue Procedure 96-32 as it agreed to during the application process. Based on the information provided, it is impossible to determine whether the homes were purchased by low, moderate or high income homebuyers and/or investors.

In 20XX, ORG brokered approximately 97 DPA transactions between buyers and sellers. Most home sales were in the \$ to \$ price range.

It is unknown whether or not ORG promoted its down payment assistance program by advising home sellers and others that sellers may claim charitable deductions on their federal income tax returns for amounts they pay to ORG. ORG refused to provide copies of any letters it may have issued or copies of any materials to verify how its down payment assistance program was marketed.

LAW

Section 501 of the Code provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided that no part of the net earnings of such corporations inures to the benefit of any private shareholder or individual. See I.R.C. § 501(c)(3).

Treasury Regulation section 1.501(c)(3)-1(c)(1) provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3). An organization must not engage in substantial activities that fail to further an exempt purpose. In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the Supreme Court held that the "presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. To meet this requirement, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

Treasury Regulation section 1.501(c)(3)-1(d)(2) defines the term “charitable” for section 501(c)(3) purposes as including the relief of the poor and distressed or of the underprivileged, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration. The term “charitable” also includes the advancement of education.

Treasury Regulation section 1.501(c)(3)-1(d)(3)(i) provides, in part, that the term “educational” for section 501(c)(3) purposes relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

Treasury Regulation section 1.501(c)(3)-1(e) provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of section 501(c)(3) if the trade or business furthers an exempt purpose, and if the organization’s primary purpose does not consist of carrying on an unrelated trade or business.

In Easter House v. United States, 12 Cl. Ct. 476, 486 (1987), aff’d, 846 F. 2d 78 (Fed. Cir. 1988) (unpublished table decision), the Court of Federal Claims considered whether an organization that provided prenatal care and other health-related services to pregnant women, including delivery room assistance, and placed children with adoptive parents qualified for exemption under section 501(c)(3). The court concluded that the organization did not qualify for exemption under section 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization’s argument that the adoption services merely complemented the health-related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization’s operation of an adoption service, which, in and of itself, did not serve an exempt purpose.

The organization’s sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. In addition, although the organization provided health care to indigent pregnant women, it only did so when a family willing to adopt a woman’s child sponsored the care financially. Accordingly, the court found that the “business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff’s adoption service is its primary goal” and held that the organization was not operated exclusively for purposes described in section 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in section 501(c)(3) because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with entities of a particular political party and that most of the organization's graduates worked in campaigns for the party's candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting the party's candidates and entities. Although the candidates and entities benefited were not organization "insiders," the court stated that the conferral of benefits on disinterested persons who are not members of a charitable class may cause an organization to serve a private interest within the meaning of Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii). The court concluded by stating that even if the political party's candidates and entities did "comprise a charitable class, [the organization] would bear the burden of proving that its activities benefited members of the class in a non-select manner." American Campaign Academy, 92 T.C. at 1077.

In Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), the court held that an organization that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops operated for exclusively charitable purposes within the meaning of section 501(c)(3). The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence collected by the Bureau of Indian Affairs or other government agencies. The organization marketed only handicrafts it purchased in bulk from communities of craftsmen. The organization did not market the kind of products produced by studio craftsmen, nor did it market the handicrafts of artisans who were not disadvantaged. The court concluded that the overall purpose of the organization's activity was to benefit disadvantaged communities. The organization's commercial activity was not an end in itself but the means through which the organization pursued its charitable goals. The method the organization used to achieve its purpose did not cause it to serve primarily private interests because the disadvantaged artisans directly benefited by the activity constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans. Therefore, the court held that the organization operated exclusively for exempt purposes described in section 501(c)(3).

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D. D.C. 20XX), the court relied on the commerciality doctrine in applying the operational test. Because of the commercial manner in which the organization conducted its activities, the court found that it was operated for a nonexempt commercial purpose, rather than for a tax-exempt purpose. As the court stated:

Among the major factors courts have considered in assessing commerciality are competition with for-profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, inter alia, whether

Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

the organization uses commercial promotional methods (e.g. advertising) and the extent to which the organization receives charitable donations.

See also, Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991) (holding that a religious organization which ran restaurants and health food stores in furtherance of its health ministry did not qualify for tax-exempt status because it was operated for substantial commercial purposes and not for exclusively exempt purposes).

Revenue Ruling 67-138, 1967-1 C.B. 129, held that helping low-income persons obtain adequate and affordable housing is a "charitable" activity because it relieves the poor and distressed or underprivileged. In Revenue Ruling 67-138, the organization carried on several activities directed to assisting low-income families obtain improved housing, including (1) conducting a training course on various aspects of homebuilding and homeownership, (2) coordinating and supervising joint construction projects, (3) purchasing building sites for resale at cost, and (4) lending aid in obtaining home construction loans.

Revenue Ruling 70-585, 1970-2 C.B. 115, discussed four situations of organizations providing housing and whether each qualified as charitable within the meaning of section 501(c)(3). Situation 1 described an organization formed to construct new homes and renovate existing homes for sale to low-income families who could not obtain financing through conventional channels. The organization also provided financial aid to low-income families who were eligible for loans under a Federal housing program but did not have the necessary down payment. The organization made rehabilitated homes available to families who could not qualify for any type of mortgage. When possible, the organization recovered the cost of the homes through very small periodic payments, but its operating funds were obtained from federal loans and contributions from the general public. The revenue ruling held that by providing homes for low-income families who otherwise could not afford them, the organization relieved the poor and distressed.

Situation 2 described an organization formed to ameliorate the housing needs of minority groups by building housing units for sale to persons of low and moderate income on an open-occupancy basis. The housing was made available to members of minority groups who were unable to obtain adequate housing because of local discrimination. The housing units were located to help reduce racial and ethnic imbalances in the community. As the activities were designed to eliminate prejudice and discrimination and to lessen neighborhood tensions, the revenue ruling held that the organization was engaged in charitable activities within the meaning of section 501(c)(3).

Situation 3 described an organization formed to formulate plans for the renewal and rehabilitation of a particular area in a city as a residential community. The median income level in the area was lower than in other sections of the city and the housing in the area generally was old and badly

Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

deteriorated. The organization developed an overall plan for the rehabilitation of the area, sponsored a renewal project, and involved residents in the area renewal plan. The organization also purchased an apartment building that it rehabilitated and rented at cost to low and moderate income families with a preference given to residents of the area. The revenue ruling held that the organization was described in section 501(c)(3) because its purposes and activities combated community deterioration.

Situation 4 described an organization formed to alleviate a shortage of housing for moderate-income families in a particular community. The organization planned to build housing to be rented at cost to moderate-income families. The revenue ruling held that the organization failed to qualify for exemption under section 501(c)(3) because the organization's program was not designed to provide relief to the poor or further any other charitable purpose within the meaning of section 501(c)(3) and the regulations.

Revenue Ruling. 20XX-27, 20XX-21 C.B. 915, in part, discusses whether down payment assistance organizations described in 3 situations operate exclusively for charitable purposes. Those described in Situations 1 and 2 are relevant to this discussion. The organization described in Situation 1 makes assistance available to low-income families to purchase decent and safe homes throughout the metropolitan area in which it is located. Individuals are eligible to participate if they are low-income and have the employment history and financial history to qualify for a mortgage with the exception that they do not have the funds necessary for down payments.

The organization in Situation 1 offers financial seminars, conducts educational activities to prepare the individuals for home ownership, and requires a home inspection report before providing funds for down payment assistance. To fund the program, the organization conducts broad based fundraising that attracts gifts, grants, and contributions from the general public. Further, the organization has policies in place to ensure that the grantmaking staff does not know the identity or contributor status of the home seller or other parties who may benefit from the sale and does not accept contributions contingent on the sale of particular properties.

Because the organization described in Situation 1 relieves the poor and distressed, requires a home inspection to ensure that the house is habitable, conducts educational seminars, has a broad based funding program, and has policies to ensure that the organization is not beholden to particular donors, the Service held that the organization is operated exclusively for charitable purposes and qualifies for exemption from federal taxation as an organization described in section 501(c)(3).

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

The organization described in Situation 2 of Revenue Ruling 20XX-27 is like that described in Situation 1 except that (1) its staff knows the identity of the party selling the home and may know the identity of other parties involved in the sale; (2) the organization receives a payment from the seller (the amount of which bears a direct correlation to the amount of down payment assistance provided) in substantially all the cases in which the organization provides assistance to the home buyers; and (3) most of its financial support comes from home sellers and related businesses that may benefit from the sale of homes to buyers who receive assistance from the organization.

Because the organization described in Situation 2 provides down payment assistance amounts that directly correlate to the amounts provided by home sellers and relies primarily on payments from home sellers and real estate related businesses that stand to benefit from the transactions to finance the program, the Service held that the organization described in Situation 2 is not operated exclusively for exempt purposes and does not qualify for exemption from federal income tax as an organization described in section 501(c)(3).

Benefiting Private Interests

Even if an organization's activities serve a charitable class or are otherwise charitable within the meaning of section 501(c)(3), it must demonstrate that its activities serve a public rather than a private interest within the meaning of Treasury Regulation section 1.501(c)(3)-1(d)(1).

Revenue Ruling 72-147, 1972-1 C.B. 147, held that an organization that provided housing to low income families did not qualify for exemption under section 501(c)(3) because it gave preference to employees of a business operated by the individual who also controlled the organization. The ruling reasoned that, although providing housing for low-income families furthers charitable purposes, doing so in a manner that gives preference to employees of the founder's business primarily serves the private interest of the founder rather than a public interest.

In *KJ's Fund Raisers v. Commissioner*, T.C. Memo 1997-424 (1997), aff'd, 166 F.3d 1200 (2d Cir. 1998), the Tax Court held, and the Second Circuit affirmed, that an organization formed to raise funds for distribution to charitable causes did not qualify for exemption under section 501(c)(3) because its activities resulted in a substantial private benefit to its founders. The founders of the organization were the sole owners of KJ's Place, a lounge at which alcoholic beverages were served. The founders served as officers of the organization and, at times, also controlled the organization's board. The Tax Court found, and the Second Circuit agreed, that the founders exercised substantial influence over the affairs of the organization. The organization's business consisted of selling "Lucky 7" or similar instant win lottery tickets to patrons of KJ's Place. The organization derived most of its funds from its lottery ticket sales. The organization solicited no public donations. The lottery tickets were sold during regular business hours by the owners of the lounge and their employees. From the proceeds of the sales

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

of the lottery tickets, the organization made grants to a variety of charitable organizations. Although supporting charitable organizations may be a charitable activity, the Tax Court nevertheless upheld the Commissioner's denial of exemption to the organization on the ground that the organization's operation resulted in more than incidental private benefit. The Tax Court held, and the Second Circuit affirmed, that a substantial purpose of KJ's activities was to benefit KJ's place and its owners by attracting new patrons, by way of lottery ticket sales, to KJ's Place, and by discouraging existing customers from abandoning KJ's Place in favor of other lounges where such tickets were available. Thus, the organization was not operated exclusively for exempt purposes within the meaning of section 501(c)(3).

Returns and Records

Treasury Regulation section 1.6001-(a) provides, in part, that any person required to file a return of information with respect to income, shall keep such permanent books of account or records, including inventories, as are sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown by such person in any return of such tax or information.

Treasury Regulation section 1.6001(b) provides, in part, that every organization exempt from tax under section 501(a) shall keep such permanent books of account or records, including inventories, as are sufficient to show specifically the items of gross income, receipts and disbursements. Such organizations shall also keep such books and records as are required to substantiate the information required by section 6033 of the Code.

Section 6033 (a)(1) of the Code provides, in part, that every organization exempt from taxation under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulation prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.

Effective date of revocation

An organization may ordinarily rely on a favorable determination letter received from the Internal Revenue Service. Treas. Reg. §1.501(a)-1(a)(2); Rev. Proc. 20XX-4, §14.01 (cross-referencing §13.01 et seq.), 20XX-1 C.B. 123. An organization may not rely on a favorable determination letter, however, if the organization omitted or misstated a material fact in its application or in supporting documents. In addition, an organization may not rely on a favorable determination if there is a material change, inconsistent with exemption, in the organization's character, purposes,

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

or methods of operation after the determination letter is issued. Treas. Reg. § 601.201(n)(3)(ii); Rev. Proc. 90-27, §13.02, 1990-1 C.B. 514.

The Commissioner may revoke a favorable determination letter for good cause. Treas. Reg. § 1.501(a)-1(a)(2). Revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 20XX-4, § 14.01 (cross-referencing § 13.01 et seq.).

ANALYSIS

ORG operates a program that (1) does not exclusively serve an exempt purpose described in section 501(c)(3) and (2) provides substantial private benefit to persons who do not belong to a charitable class.

Charitable purposes include relief of the poor and distressed. See Treas. Reg. § 1.501(c)(3)-1(d)(2). ORG's down payment assistance program does not operate in a manner that establishes that its primary purpose is to address the needs of low-income people by enabling low-income individuals and families to obtain decent, safe housing. See Rev. Rul. 70-585, Situation 1. The down payment assistance program did not serve exclusively low-income persons. Despite the representations in its application for exemption, ORG did not provide documentation verifying that there were any income limitations for participation in its down payment assistance program. ORG did not screen applicants for down payment assistance based on income. ORG's records do not include data on the buyers' incomes. Instead, the program is open to anyone, without any income limitations, who otherwise qualified for these loans.

Based on the records provided, there is no evidence that ORG's down payment assistance program limited assistance to certain geographic areas or targeted those areas experiencing deterioration or neighborhood tensions. See Rev. Rul. 70-585, Situation 4. Down payment assistance is available for any property that is otherwise able to qualify for a mortgage. Arranging or facilitating the purchase of homes in a broadly defined geographic area does not combat community deterioration or serve other social welfare objectives within the meaning of section 501(c)(3) of the Code.

Only an insubstantial portion of the activity of an exempt organization may further a nonexempt purpose. As the Supreme Court held in Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279, 283 (1945), the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. Even if ORG's down payment assistance program were directed to exclusively

Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

low-income individuals or disadvantaged communities, ORG's total reliance for financing its down payment assistance activities on home sellers standing to benefit from the transactions demonstrates that the program is operated for the substantial purpose of benefiting private parties. See Rev. Rul. 20XX-27, Situation 2.

Like the organization considered in American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), ORG is structured and operated to assist the private parties who fund it. Sellers who participate in ORG's down payment assistance program benefit from achieving access to a wider pool of buyers, thereby decreasing their risk and the length of time the home is on the market. Buyers who participate in ORG's down payment assistance program benefit by being able to purchase a home without having to commit more of their own funds. Real estate professionals who participate in ORG's down payment assistance program, from real estate brokers to escrow companies, benefit from increased sales volume and the attendant increase in their compensation. It is evident from the foregoing that ORG's down payment assistance program provides ample private benefit to the parties in each home sale.

The manner in which ORG operated its down payment assistance program shows that the private benefit to the various participants in ORG's activities was the intended outcome of ORG's operations rather than a mere incident of such operations. To finance its down payment assistance activities, ORG relies exclusively on sellers and other real-estate related businesses that stand to benefit from the transactions it facilitates. ORG provided no records to indicate that it either solicits or receives funds from other sources. ORG's receipt of a payment from the home seller corresponding to the amount of the down payment assistance in virtually every transaction indicates that the benefit to the home seller (and others involved in the transaction) is not a mere accident but rather an intended outcome of ORG's operations. In this respect, ORG is like the organization considered in Easter House which provided health care to indigent pregnant women, but only when a family willing to adopt a woman's child sponsored the care financially.

ORG's records show that ORG operated in a manner consistent with a commercial firm seeking to maximize sales of services, rather than in a manner that would be consistent with a charitable or educational organization seeking to serve one or more of the charitable purposes enumerated in section 501(c)(3). The manner in which ORG operated its down payment assistance program shows that ORG was in the business of facilitating the sales of homes in a manner indistinguishable from an ordinary trade or business. In this respect ORG's operations were similar to an organization which was denied exemption because it operated a conference center for commercial purposes. See Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 20XX).

Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

Operating a trade or business of facilitating home sales is not an inherently charitable activity. Unlike the trade or business in Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), ORG's trade or business was not utilized as a mere instrument of furthering charitable purposes but was an end in itself. ORG provided services to home sellers for which it was paid a market rate fee. ORG did not limit its services primarily to persons within a charitable class. ORG's primary goal consisted of maximizing the fees it derived from facilitating the sales of real property. ORG did not solicit or receive any funds from parties that did not have an interest in the down payment assistance transactions. Like the organizations considered in American Campaign Academy, supra, and Easter House v. U.S., 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.) a substantial part of ORG's activities furthered commercial rather than exempt purposes.

In addition, although ORG made donations to other charitable organizations from the proceeds of its down payment assistance activities, ORG's primary activity resulted in substantial benefit to private parties. Supporting other charitable organizations may be a charitable activity but the organizations operations resulted in more than incidental private benefit.

Based on the foregoing, ORG has not operated exclusively for exempt purposes, and, accordingly, is not entitled to exemption under section 501(c)(3).

The government proposes revoking ORG's exemption, effective the date of the organization's inception because the organization operated in a manner materially different from that represented in its application for exemption and additional information provided during the application process. In its application for exemption received on December 4, 20XX, ORG stated the following with respect to its objective:

"The Organization's primary objective is to increase home ownership among individuals and families unable to save enough money for a down-payment. To facilitate this objective, the Organization will provide gifts to be used as down-payments for homes in an amount of approximately three percent (3%) of the purchase price. The buyer is also encouraged (but not required) to participate in a home ownership education course. The Organization is funded primarily through collecting a service fee from the sellers or builders of the homes which are purchased by participants in the Organization's program. The down-payment gifts will be available to anyone on a non-discriminatory basis if he or she makes a proper application to the Organization. The down-payment gifts will be made with no expectation of repayment."

ORG adopted a resolution agreeing to comply with the Internal Revenue Service Revenue Procedure 96-32. Despite these representations in its application for exemption and additional information provided during the application process, ORG does not have income limitations for participants in its down payment assistance program and did not provide any records to verify

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name XX = Date XYZ = State
 President = president Address = address Motto = motto

that it screened applicants for down payment assistance based on income. The records provided by ORG did not include data on the buyers' incomes and gave no indication that ORG screened on such data. Rather, ORG's down payment assistance program provided "gifts" to any homebuyers who qualified for a loan. Revocation of a determination letter may be retroactive if the organization operated in a manner materially different from that originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 20XX-4, § 14.01. ORG's operation of its down payment assistance activities in a manner materially different from that represented in its application for exemption justifies retroactive revocation of ORG's determination letter.

Conclusion:

ORG does not operate exclusively for an exempt purpose as required of an organization described in section 501(c)(3). ORG provides down payment assistance, purportedly in the form of a gift, to individuals and families for the purchase of a home. ORG offers its down payment assistance to interested buyers regardless of the buyers' income levels or need. ORG's down payment assistance activities do not target neighborhoods in need of rehabilitations or other relief such as lessening neighborhood tensions or eliminating prejudice and discrimination.

ORG operates a trade or business in a commercial manner rather than to serve charitable purposes. Its activities further the private interests of home sellers and other real estate related businesses. ORG's primary activity is brokering transactions to facilitate the selling of homes. ORG's brokering services are available to homebuyers, sellers, realtors, lenders, home builders, and title companies regardless of the buyers' income levels or need and regardless of the condition of the communities in which the homes are located. Alliances are built with the realtors, lenders, home builders, and title companies to assure future business for the mutual benefit of the participants. Because ORG's primary activity is not conducted in a manner designed to further section 501(c)(3) purposes, ORG is not operated exclusively for exempt purposes within the meaning of section 501(c)(3).

In addition, ORG's inability and/or refusal to produce documents requested indicates that the organization did not exercise ordinary business care and prudence in meeting its obligation to keep and produce such records and comply with IRS rules and regulations as required.

For the foregoing reasons, revocation of exempt status is proposed. Because ORG operated in a manner materially different from that represented in its Form 1023 application the government proposes that the revocation be effective retroactively to the date of the organization's inception.

Organization's Position

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX12

LEGEND

ORG = Organization name

XX = Date

XYZ = State

President = president

Address = address

Motto = motto

ORG's position with respect to the issues, facts, applicable law and government's position as discussed in this report is unknown. ORG will be allowed 30 days to review this report and respond with a rebuttal if considered necessary.